The Administration of Income-tax in India

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The Income-tax in India has, so far, not proved to be as elastic a source of revenue as it is in other countries. Direct taxation on income is unpopular among the Indian trading and professional classes, and moreover the task of accurate assessment which is essential for a high graduated rate of income-tax has always presented great difficulties in the peculiar conditions of India. The law has recently been modernised and an efficient administrative machinery for the assessment and collection of the tax has been organised.

There has been no decrease in the rate of income-tax and supertax after the War, which still stand at as high a level as they have ever stood in India. The tax is one which, at any rate, for some years to come, can hardly be raised to meet emergencies. With a view to place the Indian Income-tax on a more scientific basis it is necessary to improve the machinery for the assessment and collection of income-tax as well as the basis and structure of the system. Attention may therefore be drawn here primarily to the necessary improvements in the administration of income-tax.

1. SOME ASSESSMENT ANOMALIES

The Income-tax Report 1932-33 as compared with the results of 1930-31 discloses certain points of interest. What with an increase in rate and a surcharge of 25% the income-tax demand went up by about 25% while the supertax demand went down by 25%. This seems to indicate some drastic change in the incidence of the tax and a reference to further tables shows that while the taxed income of companies went down from 42 to 24 crores and of registered firms from 7½ to 5 crores, the income of Hindu undivided family and other income excluding salaries, interest and so on, which means the income of the small assessee has actually been held to have gone up during the 2 years. The number of individuals paying supertax has increased from 1,477 to 2,677 and of unregistered firms has increased from 228 to 258 while the number of companies has gone down from 892 to 625. The meaning of these figures is plain. Companies submit audited accounts which virtually have to be accepted and their figures may be taken to tell the truth. How is it that the results from other sources are so different ? It is not that the net has been cast wider and there are more assessees, for, neglecting the below 2,000 classes, the number

of assessees has gone down from 318,000 to 298,000. We believe it is due to the growing severity of the administration of the Act.

If we take the Bengal Income-tax figures for 1933-34, the outstanding fact in the report is that it is the assessee who earns between 3,500 and 7,500 rupees per annum who is the backbone of the province and so large is his preponderance that in spite of the fact that higher classes of assessees pay higher rates, he is the backbone of the tax-paying classes. Whether we deal with salaried persons, Hindu undivided families, unregistered firms, associations of individuals or just individuals earning their own living, in each case the maximum of earnings goes to the grade earning Rs. 5,000 to Rs. 7,500 per annum. As between individuals and salaried people, this does not seem to call for much comment. The chances of earning in a salaried post are set off against the chances in independent careers and one would expect some sort of correspondence in the ordinary average person, but that the income of unregistered firms which may have 2 or 3 partners or associations of individuals which may consist of 30 or 40 persons should be greater in this grade than in any other seems a subject very fit for further investigation. Still more remarkable is the fact that the Hindu undivided family, which must also have several members, crowds round this income level. Very noticeable too is the way in which the total income of all assessees in the Rs. 40,000 to Rs. 50,000 class is much less than the total income either in the Rs. 30,000 to Rs. 40,000 class or the class above Rs. 50,000. Exactly the same thing happens in the Rs. 12,500 to Rs. 15,000 class. The total income here is appreciably less than in the Rs. 10,000 to 12,500 class or the 15,000 to Rs. 20,000 class. And this holds not for the assessees as a whole, but for each class of assessee separately. The total incomes in each item are so much alike as to say that they are identical. The earnings of the Rs. 1,000 to Rs. 1,500 class are high, whether salaried men, Hindu undivided families, unregistered firms, associations of individuals or individuals. These figures fall for 3 out of 5 from that grade, and for all five from Rs. 1,500 to Rs. 2,000 grade until the Rs. 3,000 to Rs. 3,500 grade is reached. Thereupon all classes fall until the Rs. 12,500 to Rs. 15,000 level comes when they all go up again in the Rs. 15,000 to Rs. 20,000 grade only to fall unanimously till Rs. 30,000 is reached and then all unanimously up to Rs. 40,000 and down to Rs. 50,000. What is the explanation for this remarkable state of affairs ? It is worth investigation.

As regards the insurance question, tax rebates on account of insurance premiums amount to 4½ lakhs. Return IV on page 8 shows when these rebates are claimed and in none of the ordinary

grades does the maximum rebate claimed exceed more than about 3% against the 16% allowed by Government. There is probably about 25 lakhs of unused concessions going to waste every year which is enough to explain quite a lot of persuasiveness and ingenuity on the part of Insurance Companies.

Out of 19,000 returns filled by companies and non-salaried assessees, only 2,598 were accepted as correct, and out of 28,000 sets of accounts produced only 17,500 were adequate enough to base an assessment on them. These are eloquent figures to bear testimony to the restraint of the department in refraining from any prosecutions at all.

On the other hand, assessments under Section 23 (4) seem to be 5% on the average and there is no doubt that such assessments are heavily penal. This is a matter in which the Central Board counsels moderation in its Manual and a friendly and helping hand on the part of the Income-tax officers would avoid most of these cases. The section brings odium on the Department. If its officers would explain to assessees the consequences of their failure to make returns, this would be avoided.

The official belief that for every assessee there are three who escape is probably very near the mark. The real solution for this is the growth of public opinion. The assessee is far from realising that he is paying for those who escape. While there is insufficient effort to rope in new tax-payers, there is far too much effort to make existing assessees pay as much as or more than before, and while admitting all the difficulties, we make no apologies for suggesting that a thorough reorganisation is required.

It is a commonplace among Europeans that the tax bears hardly upon them in particular because they do not escape. Europeans are interested mainly in salaries and dividends and so these figures belie the popular theory. The man who is suffering now is the Indian assessee who is on the list. This is not to say that there are not enough on the list but those who are, are obviously being squeezed. To turn to another point. As regards the return showing the number of assessees, in Bengal there are 8,700 assessees in the 2,000 to 2,500 grade and 5,000 in the 2,500 to 3,000 grade and these figures are somewhat incredible. On the average income the tax can under certain circumstances be more severe in India than in England, and it is to the interest of all of us that every possible assessee should be enrolled.

Applications to the High Court are few. This is also an indication of the difficulty of getting to the Court because so many

matters in dispute are held to be questions of fact rather than of law, and once an Income-tax Officer comes to the conclusion on a question of fact, his superiors have the greatest reluctance in differing from him. In the criminal law administration, consultations between a Magistrate and the authority to whom an appeal will go are unknown. In the Income-tax Department they are the rule rather than the exception and confidential notes which the assessee has no opportunity of seeing but which bind the Income-tax Officer completely are very common. This is a most objectionable practice and it is because of this, the demand for an independent appellate authority is gaining strength.

2. INCOME-TAX FIGURES

The figures furnished by the Department are fairly full. We should, however, like to see added statements showing province by province the number of assessments under Section 23 (4) and the number of cases in which the use of Section 13 is invoked. These are the sections which cause most injustice and in the case of illiterate assessees, in particular, there is a danger of the tax becoming a tax on turnover and there are no arguments for imposing a tax on turnover under the guise of a tax on profits.

Finally, what is needed is some way of curing the Income-tax Officers of their ineradicable optimism as to the ease with which profits accrue. It is not really possible in any ordinary line of competitive business in India to make more than 10 to 20% net profit on capital. As soon as there are signs of more being likely, the business becomes overcrowded. This elementary fact finds no recognition in the Department.

3. INCOME-TAX AND THE PROVINCES

Recently in answer to a question in the Council of State regarding the amount of Income-tax collected in the Provinces, the Government submitted a statement and the figures as published in the daily papers are as under :—

Madras	..	1,67,98,748	lakhs.
Bombay	..	4,62,23,157	,,
Bengal	..	4,39,80,242	,,
United Provinces	..	1,16,00,377	,,
Punjab	..	86,90,484	,,
Burma	..	1,74,16,122	,,
Bihar and Orissa	..	68,71,745	,,
C.P. & Berar	..	38,53,422	,,
Assam	..	19,39,754	,,
N. W. Frontier Province	..	11,73,980	,,

These figures for 1932-33 seem to be of special interest for more than one reason, for they show considerable changes in comparison with the figures of previous years which are given below:—

	1924-25.	1925-26.	1926-27.	1927-28.	1928-29.	1929-30.	1930-31.
Madras	130	137	128	134	131	134	132
Bombay	404	315	321	324	318	369	343
Bengal	555	504	570	488	615	618	557
U.P.	79	80	74	83	90	90	88

The first obvious fact is that the figures of the year 1932-33 reveal how much more seriously hit Bengal industries have been than have been the industries of other provinces.

These figures of Income-tax collections are interesting for another reason, i.e., the problem of the division of the proceeds of the taxes on income between the Provinces and the Central Government that was examined by the Percy Committee. In its recommendations, that Committee suggested a method of distribution which if it were ever accepted, would inflict upon Bengal an even greater injustice than the Meston Settlement. Therefore a scheme of distribution (of the Income-tax proceeds) which pays due regard to wide fluctuation in industrial profits would prove much fairer to Bengal and other provinces which are principally affected by industrial profits.

4. SUPER-TAX

Super-tax is a taxation anomaly. In framing future taxation Government might take the business community into their confidence in order to avoid some of the present glaring anomalies. By reason of the levying of a super-tax on the profits of Companies, as an additional Income-tax but on a different basis, they got the ludicrous position, in the case of a company which has Preference Shares on which the dividends exceed half a lakh of rupees, that the taxation which is borne by the holders of the Ordinary Shares of that company is so arranged that the smaller the rate of dividend earned on the ordinary shares the higher is the rate of taxation. This situation is to be found in the case of Spencer and Co., Ltd., Madras. A much fairer way of taxing companies would be to incorporate the super-tax in the Income-tax, and so also should be incorporated any additional levies for Provincial Revenues. This

might mean a uniform higher rate of Income-tax on Companies and no super-tax on Companies, but all shareholders, whether Preference or Ordinary, would bear their fair quota of a Company's taxation and the Ordinary Shareholders would not be penalised as they are now.

The Income-tax Act is badly drafted. To give one instance, the Bihar and Orissa Income-tax Department (June 1933) attempted to seize property belonging to a limited company of which the assessee is the Manager, and the Commissioner also thought of a body warrant to extract payment of a sum which he ought to know cannot be paid and which he does know ought never to have been asked for. This is all due to the bad drafting of the Income-tax Act, but it caused no particular trouble when the scale of taxation was small. Now that the scale is appallingly high, the Act is a menace to every one, and unless the Income-tax Department is able to administer it so that injustices of this sort do not occur, the Department will become violently unpopular.

It is often said that the Indian Penal Code drafted by the great Macaulay casts its net so wide that even the most upright man commits breaches of it everyday. Nevertheless it stands almost unaltered, and the reason is that it is interpreted reasonably. The Income-tax Department may be invited to draw the obvious moral. With the *non-possumus* attitude of the Central Board no one can have much sympathy. They are no doubt technically right, but we do not want administrators who worry over much about technicalities. Let us have a little humanity. The real root of the trouble, however, is the Commissioner of Income-tax. He has ample powers of redress and he ought to use them properly.

5. BAD DEBTS

Another Income-tax rule has been added recently to the growing list designed to separate one big hole into two small ones. Take the question of *bad debts*. This is largely a matter of commercial practice, but as the result of an upcountry decision good commercial precedent has now little or nothing to do with the matter, for it has become a rule of the Department that bad debts are not allowed as a deduction against profits unless an attempt has been made to recover them by legal proceedings. It is an ordinary sound commonsense maxim that it is no good throwing good money after bad and no one in their senses will attempt to recover money by expensive legal proceedings when they know the debtor cannot pay. But unless they are prepared to do so, they cannot hope

for any Income-tax relief and the result is that the Department takes very large sums which are in no way profits but rather losses.

About 3 years ago, an Income-tax Bill was introduced by Sir Hari Singh Gour in the Legislative Assembly aiming at providing for the association of non-officials with Income-tax Officers in deciding the cases of assessees. But such a machinery may be very cumbrous and expensive and a simple way was to provide for a non-official Court of Appeal both on matters of fact and matters of law which would be made much more accessible than the High Courts to which only matters of law can be referred. The processes of application to the High Court are cumbersome and expensive and far too dependent on the opinions of the Commissioners of Income-tax.

The growing stringency in tax-collecting circles has been such and the need for some sort of independent control of the taxing authorities has been such that it is rapidly becoming one of the foremost problems of reform. The real trouble lies in the fact that the taxing authorities are expected to interpret the law judicially but also with an eye to the main chance, namely revenue. The cry for separation of executive and judicial functions has long been insistent, but that affected only the public which came within the scope of the criminal law. Every one earning more than Rs. 1,000 per year comes within the ambit of the Income-tax law which has become by far the most important law in India, and without expressing any opinion about the separation of the executive and judicial functions of the ordinary sort, we believe that there is the greatest need for it in this Department.

As the Act is badly drafted and complicated, attempts to remove big loopholes of escape usually result in a set of smaller holes. Each Provincial High Court is putting out rulings which are often contradictory and which have to be followed or discarded by the Department according to their sense of fitness of things. If there are discrepancies, they usually follow the ruling which is against the assessee, rather than the one in his favour. Of course the Income-tax Department encounters very great difficulties over the many and varied systems of book-keeping in this country, and the work both of examiners and Income-tax Officers has reached a particularly high level of technical excellence. They know their Act and rulings and show surprising ability in ferreting out relevant information from the most complicated accounts.

The Income-tax Officer, however, having got his facts before him, has to apply the law to them judicially and from his rulings there is an appeal to the Assistant Commissioner, and under certain circumstances, to the Commissioner. Both these appeals should be conducted judicially and we have no hesitation in saying that the very frequent consultations of the Assistant Commissioners by the Income-tax Officers, before they pass orders, rob the assessees of all hope of an independent appeal and is entirely contrary to the ordinary British system of administration of law.

What would happen if a Munsif consulted a District Judge before passing judgment in a Civil Suit? What would the High Court say? Yet exactly this happens every day in Income-tax circles and we do not think the authorities will deny it. Any complicated case is taken by the Income-tax Officer to the Assistant Commissioner, with the result that if there is an appeal, the latter has already made up his mind. Practically it is no appeal at all. The disadvantage is particularly felt when an assessee succeeds in getting a case referred back for reassessment and the greatest difficulty comes when an assessee has paid his tax and hopes for a refund. We do not blame the Income-tax Officer, because he is an executive officer and his primary duty is to see that taxes are collected, and if possible, revenue is increased. Nor is the Assistant Commissioner in a very different position though his higher status should make him better able to assert his opinions and work judicially when that is expected of him. The defect lies with the whole system. The Income-tax officer knows that his work is judged largely by his success in taxing. If he agrees to accept the assessee's contentions and there is no appeal, he knows that there is every chance of his records coming under the scrutiny of the Assistant Commissioner or the Commissioner and unless the Income-tax officer is prepared to show that his assessment is correct by means of a very voluminous note based often on very complicated accounts and facts, the man higher up, who is himself under the necessity of seeing that revenue comes in, must always wonder whether his staff are getting all they should. This is no reflection on the staff. It is the result of the system.

The time is come when it is necessary to have from the Assistant Commissioner grade upwards two parallel organisations, one for taxing and the other for hearing appeals. If the Income-tax officer is in doubt as to the proper interpretation of the Act, he may refer to the Commissioner, but let the assessee, who is aggrieved by an order, feel that he has a genuine appeal to make to an officer who has no concern with the state of the revenue and

is charged only with the duty of interpreting the law without favour in exactly the same way as the civil courts are charged. Only by this means is it possible to secure fair play. Let the *Judicial* Assistant Commissioner, as we call him, be free for all dependence on the Executive Assistant Commissioner or the Central Board of Revenue. In the end, the successful administration of the Income-tax depends on the support of the public, and a reform such as this would go far to enlist that support.

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